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SUBJECT: NEW INVESTMENT LAW DRAWS BOTH PRAISE AND CONCERN

REF: KABUL 000497

Summary

1. (SBU) A new investment law, quietly signed by the President just before the new Parliament convened, has elicited both praise and concern among the international and Afghan business community. The new law, while offering more favorable conditions in areas such as the leasing of real estate and duty-free export of goods manufactured in Afghanistan, also excludes permanent private sector representation on the High Commission for Investment, leaves open the possibility of the establishment of a minimum threshold value for investment, and includes language that may foster corruption in the consideration of proposals in sensitive sectors such as mining and hydrocarbons. End summary.

2. (U) The Government of Afghanistan passed a new investment law in early December, squeezing it in just before the new Parliament sat on December 19, after which laws could no longer be passed by decree. This law replaces the 2003 Law on Domestic and Private Investment, which was considered emergency legislation.

3. (SBU) Donors and GOA officials have long agreed that a more comprehensive law was needed. In the last year, multiple drafts have circulated for comment among the donors. The GOA had been under pressure to pass several
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pieces of key economic and commercial legislation before Parliament convened and the legislative process slowed as members got their bearings. Minister of Commerce Arsalas announcement of the laws passage during the December 4 Trade and Investment Framework Agreement talks took us by surprise, as the lead-up to passage was unusually quiet. (Note: In the past, a hurried circulation of a final or near-final draft of a key piece of legislation provided donors a final opportunity to comment. End note.) The law was passed in Dari and Pashto only and an official English translation is still not available.

Similarities

4. (U) As in the old law, the new legislation allows both foreign and domestic investors to make investments, establish joint ventures or sole ownership enterprises, freely transfer profits abroad and freely sell or divest their enterprise. It also continues to allow for the expropriation of the assets of an enterprise by the State
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for the purpose of public interest and on a non-discriminatory basis.

And Differences

5. (U) Differences are as follows:

--The composition of the High Commission on Investment has been altered. It now includes the Governor of the Da Afghanistan (Central) Bank (DAB,) as well as the Minister of Agriculture. Previously, representatives of the private sector were allocated two seats; the new law does not allow for permanent representation, specifying that the Commission is authorized to invite representation from the private sector to provide consultation and comment when and if desired.

--More detailed rights and responsibilities have been allocated to the Commission, including the right to establish a threshold value for initial capital investment (for both foreign and domestic investors) and the ability to authorize the Afghan Investment Support Agency (AISA) to register businesses that fall below this threshold value.

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While the text in the old law refers to the Commission as the focal point for policymaking, the new law identifies it as the highest governing authority in policy-making on investment.

--Areas in which foreign investment can be limited by the GOA or restricted by special legislation have been expanded. These areas now include: non-banking finance activities, insurance activities, infrastructure (defined as power generation or transmission, water delivery or treatment, sewage, waste-treatment, airport, telecommunications, health and education facilities) and natural resources (oil, gas, minerals, metals and forests.)

--Individuals or companies interested in investing in the above sectors may, however, submit a proposal for consideration on a case-by-case basis by the Commission and relevant Ministries. Such investment may be subject to conditions that are more restrictive than outlined in the Law. This provision does not apply to existing investment.

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--The responsibilities of AISA have been spelled out clearly. According to the Law, AISA has the responsibility to establish procedures for the submission, review and registration of applications for foreign and domestic investment, to review the applications, to register the enterprises and monitor them, to promote and attract foreign investment in Afghanistan and to ensure compliance with the Law.

--An ad-hoc reporting requirement, previously only sporadically enforced by AISA, is now required. Registered enterprises must immediately notify AISA if there have been any changes in ownership or capital structure and file an Annual Update (a form which currently includes capital invested, number of employees, profits and losses, etc.) Enterprises that do not comply risk losing their licenses.

--Income tax concessions for loss carry forward and an accelerated deduction for depreciation on capital assets, as allowed for in the Income Tax Law, have been included. Exemption from export duties for goods manufactured in Afghanistan has been expanded indefinitely; under the previous law, this exemption covered companies for only four years from the date of first manufacture.

--A foreign enterprise may lease real estate up for to 50 years, instead of the 30 allowed under the previous law.

--Investors are entitled to expanded options for dispute resolution. The previous law allowed for dispute resolution in accordance with the United Nations Commission on International Trade and Laws rules or through the International Center for Settlement of Investment Disputes. The new law also permits an investor to specify a particular arbitration or dispute resolution procedure in a contract or agreement, including specifying that arbitration may take place outside of Afghanistan and that a law of jurisdiction other than Afghanistans may apply.

--The law allows for expropriation only for the purposes of public interest, as in the previous law, but expands upon
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compensation provided for such appropriation, as well as methods of disputing the expropriation.

COMMENT

16. (SBU) The new legislation has been met with mixed reactions from both foreign and Afghan businesses and is viewed by some as seriously flawed in several key areas. The language on threshold value for investment is open-ended, allowing the Commission to decide at a later date whether or not it wishes to establish such a value, as well as the mechanism for approval of investment both above and below the value. Several donors had recommended that this language be excised from earlier drafts. The exclusion of the private sector from permanent representation on the High Commission for Investment is troubling; previously, representatives enjoyed two rotating seats. The private sector has few formalized avenues of communication with the government on matters that impact its development and its exclusion from the Commission will exacerbate this problem. The inclusion of the DAB on the Commission is unusual; the participation of Governor of an independent central bank could create a conflict of interest.

17. (SBU) The formalization of AISAs duties is a positive milestone in the development of a very effective organization. The language regarding the duties and responsibilities of the Commission, meanwhile, is vague.

Offering expanded options for dispute resolution is a progressive step. However, it is likely that only investors seeking very large damages would exercise the option to seek dispute resolution outside of the country. This mechanism does not mitigate the urgent need to reform the largely-defunct commercial court system. The reaffirmation of certain income tax concessions has been received positively, as have been the expanded terms for the lease of real estate and export duties on goods manufactured in Afghanistan. The new law, however, fails to clarify language allowing for expropriation of assets by the State for the purposes of the public interest, which could serve as a significant deterrent to investors, both foreign and domestic. Additionally it does not address how fair-market value will be determined in the case of such an expropriation.

18. (SBU) Perhaps of most concern is the language regarding restricted areas of investment. This language is not in accordance with WTO investment guidelines and will ultimately need to be revised as part of the GOAs accession bid. It is also very broad and could create a high degree of uncertainty for potential investors. Some experts warn that the process of vetting these proposals through a mini-cabinet, under guidelines that are vaguely defined, opens to the door for corruption. Reftel reports that this may already be occurring. Post has and will continue to advocate for transparent regulations and processes for investment in all areas that will be consistent with international best practices.

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